No. 16257

In the United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA, APPELLANT

v.

FRANK N. MATTISON and IDA G. MATTISON, APPELLEES

On Appeal from the Judgment of the United States District Court for the District of Idaho

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BRIEF FOR THE APPELLANT

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CITATIONS

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OPINION BELOW

The opinion of the District Court (R. 21-31) is reported at 163 F. Supp. 754.

JURISDICTION

This appeal involves federal income taxes for the year 1952. The taxes in dispute were paid on July 2, 1956. (R. 41.) Claim for refund was filed on July 10, 1956 (R. 9-10), and no action thereon was taken by the Commissioner (R. 5, 14). On February 8, 1957, within the time provided in Section

3772 of the Internal Revenue Code of 1939, the taxpayers brought an action in the District Court for recovery of the taxes paid. (R. 3-12, 219.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1346. The judgment of the District Court was entered on July 29, 1958. (R. 48-49.) Within sixty days and on September 26, 1958, a notice of appeal was filed. (R. 49-50.) Jurisdiction is conferred on this Court by 28 U.S.C., Section 1291.

QUESTION PRESENTED

Whether the District Court erred in failing to hold that, on the undisputed facts of the case, tax consequences must be resolved in the light of the established rule that a purchase of corporate stock for the purpose of acquiring the corporate assets through liquidation of the corporation is to be treated as a purchase of the corporate assets, rather than of the corporate stock.

STATUTES INVOLVED

Internal Revenue Code of 1939:

> SEC. 115. DISTRIBUTIONS BY CORPORATIONS.
>
> * * * *
>
> (c) *Distributions in liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. * * *
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> * * * *
>
> (26 U.S.C. 1952 ed., Sec. 115.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

* * * *

(4) [as amended by Sec. 150 (a) (1) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Long-term capital gain.*—The term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 6 months, * * *

(26 U.S.C. 1952 ed., Sec. 117.)

STATEMENT

The taxpayers, husband and wife, who filed joint returns on the cash basis for the calendar years 1952 and 1953 (R. 32), brought this suit to recover $53,461.89 in income taxes (including interest) which they had paid for the calendar year 1952 pursuant to a net deficiency determination for 1952 based on the ground that certain transactions should be treated according to their substance as a purchase of corporate assets, rather than of corporate stock, and therefore as resulting in *short*-term capital gain in 195*2*, rather than in long-term capital gain in 195*3*.[1] The District Court entered judgment in favor of the taxpayers. (R. 48-49.)

The facts as found by the District Court (R. 32-45) may be summarized as follows:

Wescott Oil Company was incorporated in 1920 under the laws of Idaho and thereafter for more

[1] The deficiency for 1952 is a *net* deficiency, as already noted, in the amount of $43,397.81, which is the difference between the additional taxes determined for 1952 and the overpayment determined for 1953. (See R. 41.)

than thirty years engaged in the business of selling gasoline and related petroleum products in Idaho and Oregon. The corporation was wholly owned by the Continental Oil Company until 1926, in which year C. J. Wescott acquired 20% of its stock and became president of the Company, which position he held until its dissolution in June, 1953. In 1945 Continental sold its stock in Wescott Oil to Mr. Wescott who in turn resold a considerable amount thereof to friends and associates at the same price he paid Continental therefor. At that time the taxpayer (Mr. Mattison), who has been secretary-treasurer of Wescott Oil from 1929 to 1952, acquired 25 shares of stock of Wescott Oil. (R. 33.)

During the considerable number of years that Wescott Oil was in existence, its name was well known in Idaho and parts of Oregon and it was a very successful venture earning sizable profits and paying dividends. (R. 33.)

In about 1950, Mr. Wescott and the other stockholders—for business reasons not particularly important here—resolved to dispose of their shares of stock in Wescott Oil provided a satisfactory price could be obtained therefor. Mr. Wescott, in behalf of himself and the other stockholders, undertook to find a buyer for these shares. (R. 34.)

In 1951 Mr. Wescott entered into negotiations with Continental for the sale of the stock of Wescott Oil. For a while it looked as though the negotiations would be successful, but they failed because Continental was unwilling to pay the price of $607.63 a share demanded by the stockholders for their stock (a price deemed necessary to net the stockholders

$500 a share after paying taxes on their capital gains). (R. 34-35.)

The taxpayer, having been present at some of the negotiations with Continental and being aware that the negotiations had failed, in April of 1952 approached Mr. Wescott in regard to purchasing the stock of Wescott Oil at the same price Mr. Wescott had been asking for it from Continental. Mr. Wescott and the taxpayer orally agreed that the taxpayer could acquire the shares at the same price they had been offered to other prospective purchasers. (R. 35-36.)

Immediately after receiving this oral assurance from Mr. Wescott, the taxpayer began negotiations for the sale of the operating assets of Wescott Oil to Continental, if and when he acquired them. After some negotiations, Continental on May 12, 1952, executed a binding offer in favor of the taxpayer, good for thirty days, to purchase the operating assets of Wescott Oil for $1,000,000, plus inventory. After obtaining this purchase agreement, the taxpayer approached other stockholders of Wescott Oil and obtained written options to purchase their shares in the corporation. During the remainder of May 1952 the taxpayer obtained options from the sixteen stockholders of the corporation other than Mr. Wescott and himself. These options were exercised in writing on or about May 30, 1952, and pursuant to the terms thereof the other stockholders of Wescott Oil deposited their shares with the First Security Bank of Idaho (hereafter called the Bank) as escrow holder. (R. 36.)

On June 10, 1952, all of the outstanding stock of the Wescott Oil Company, except the shares owned by the taxpayer, had been deposited with the Bank. As permitted under the escrow instructions, Wescott Oil issued a new certificate of stock on June 10, 1952, in the name of the taxpayer, Frank N. Mattison, for the total of 2,189 shares. This new certificate represented all the stock which the taxpayer had contracted to purchase from the other stockholders as well as the 25 shares which he had purchased in 1945, and constituted all the outstanding stock of Wescott Oil. (R. 36-37.)

On June 13, 1952, the taxpayer, being the sole stockholder of Wescott Oil, called a special meeting of the stockholders at which it was resolved that the business of the corporation be discontinued and that the officers and directors proceed to wind up its business affairs, transfer its assets to the taxpayer, the sole stockholder, and dissolve the corporation. Immediately following the stockholders' meeting, a special meeting of the directors of Wescott Oil was held at which time the taxpayer resigned as secretary-treasurer of the Company and the directors resolved that the operating assets of Wescott Oil should be conveyed to the taxpayer by way of a partial distribution in liquidation. Accordingly, on June 16, 1952, Wescott Oil conveyed its operating assets to the taxpayer, who in turn reconveyed such assets to a wholly-owned subsidiary of Continental. (R. 37.)

As partial consideration for the conveyance of these assets, Continental on the same date, June 16, 1952, issued a check to the taxpayer for $1,400,000,

which he endorsed over to the Bank. The proceeds of this check were applied as follows: $265,000 paid on the obligation of the Company to the Bank which had been personally assumed by the taxpayer, and $1,135,000 paid out to the selling stockholders under the escrow instructions. The remaining portion of the purchase price for the operating assets of Wescott Oil ($289,399.07) was paid to the taxpayer by the wholly-owned subsidiary of Continental on June 27, 1952. Of such sum, the taxpayer made the following disbursements: $45,123.89 in final payment of the indebtedness of Wescott Oil to the Bank personally assumed by the taxpayer, and $212,480.57 in final payment for the shares which the taxpayer had purchased from Mr. Wescott. After these disbursements, $31,794.61 was left. (R. 38.)

The certificate representing all the stock of Wescott Oil as issued to the taxpayer on June 10, 1952, was released to him by the Bank with the following legend endorsed thereon (R. 38-39):

> June 16, 1952, partial liquidation made this date hereon by distribution to the above-named stockholder, Frank Mattison, of all the real and personal property, investments, fixtures, equipment, contracts, and other valuable rights and liabilities, and all merchandise, accounts and notes receivable of the company excepting only cash and stock of Lilly Seed Co. This stock being hereafter nontransferable, all pursuant to stockholder's and directors' resolution of June 13, 1952.

The taxpayer retained the stock certificate in his

possession until he surrendered it to the corporation for cancellation in June of 1953. (R. 39.)

Subsequent to the conveyance of the operating assets of Wescott Oil to the taxpayer and by him to the subsidiary of Continental on June 16, 1952, Wescott Oil continued to wind up its business affairs until May 12, 1953, at which time the balance of the assets of the corporation, then consisting of cash in the amount of $101,585.76 was distributed to the taxpayer, and he in turn surrendered for cancellation the certificate which he held representing all the outstanding stock of the corporation, which was thereupon cancelled. Wescott Oil was finally dissolved by court decree on June 19, 1953. (R. 39.)

Subsequently, on November 3, 1953, the taxpayer received shares of stock in the Lilly Seed Company, which he sold in 1955 for $1,000, and an insurance refund in the amount of $275.90. (R. 40.)

All of the formalities incidental to a bona fide purchase of Wescott Oil stock and a liquidation of the corporation were observed. (R. 43-44.)

The only unusual factor in taxpayer's purchase of the stock of Wescott Oil was that at the time of purchasing the stock he intended to liquidate the company at a profit. Distributing to himself and reselling the operating assets of the company was an essential part of his plan for liquidation. (R. 45.)

The 2164 shares of Wescott Oil stock purchased by the taxpayer in May of 1952 cost him $1,347,480.57 and the 25 shares he had previously acquired in 1945 cost him $4,841.25. Hence, the total cost of all the stock was $1,352,321.82. (R. 40.)

The parties are agreed that the taxpayer's total gain was $126,099.78. (R. 42.) This is the amount which results from the following computation:

RECEIPTS:		
Sale price of Wescott Oil operating assets to Continental, which is also the fair market value of those assets (R. 40)	$1,689,399.07	
Cash received in liquidation of Wescott Oil in May of 1953 (R. 40)	101,585.76	
Lilly stock and insurance refund received in November of 1953 (R. 40)	1,275.90	
		$1,792,260.73
DISBURSEMENTS:		
Cost of all of the Wescott Oil stock (R. 40)	1,352,321.82	
Obligation of Wescott Oil to Bank personally assumed by taxpayer (R. 40)	310,123.89	
1952 expenses (R. 40)	3,677.07	
1953 expenses (R. 41)	38.17	
		1,666,160.95
		$ 126,099.78

The controversy is as to how and when a portion of that gain is taxable. In their joint tax returns the taxpayers treated the transactions involved as a purchase of corporate *stock* from which capital gain was realized over and above the cost of the stock as and when received in liquidation of the corporation. Thus, in their 1952 joint return they reported capital gain of only $23,276.29 and in their 1953

return reported capital gain of $102,823.49 (the $101,585.76 received in May of 1953, plus the $1,-275.90 in Lilly stock and insurance refund received in November of 1953, less $38.17 in expenses). The $102,823.49 was reported as *long*-term capital gain, as was the portion of the $23,276.29 for 1952 which was attributable to the 25 shares of Wescott Oil stock which the taxpayer had owned before the transactions involved here.[2] (R. 40-41, 43.) The Commissioner's deficiency determination for 1952 (and determination of an overpayment for 1953 (R. 41)) resulted essentially from changing the manner of treating the amount of $101,585.76 which the taxpayer reported as long-term capital gain in 1953. (R. 41.) The Commissioner switched that amount to 1952 income and treated (1) as *long*-term capital gain, the portion attributable to the 25 shares of Wescott Oil stock which the taxpayer had owned since 1945 and (2) as *short*-term capital gain, the remaining portion attributable to the taxpayer's 1952 purchase of 2,164 shares and liquidation of the corporation. (See R. 11-12, 42, 47.) The result was a determination that the taxpayer owed additional taxes in the amount of $69,257.45 for 1952 and was entitled to a refund of $25,859.64 for 1953. This net deficiency of $43,397.81, with interest in the amount of $10,064.08, was paid by the taxpayer and

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[2] The remaining portion of the $23,276.29, reported as short-term capital gain (R. 40), was necessarily short-term capital gain in 1952, since taxpayer had not held for six months either the Wescott Oil stock he purchased in 1952 or the operating assets of Wescott Oil he received and sold to Continental in 1952.

is the amount which he sought to recover in this suit for refund. (R. 41.)

The District Court held that the entire amount of the gain reported by the taxpayer in 1953 as long-term capital gain was properly reported. (R. 47.) Thus, the District Court allowed recovery of the taxes in suit (R. 47) despite the Government's contention that the taxpayer's 1952 purchase of 2,164 shares of Wescott Oil stock and liquidation of the corporation had substance only as a purchase of the *assets* of the corporation (R. 26-29) from which the taxpayer, when he sold the operating assets in 1952, realized short-term capital gain in the amount of the difference between (1) the amount received on the sale of the operating assets in 1952 and (2) that portion of the cost of the 2,164 shares which is allocable to and is the taxpayer's basis for the operating assets.

STATEMENT OF POINTS TO BE URGED

The Government's statement of points is contained in the record at pages 224-225. Briefly, it is our position that the District Court erred in failing to apply, to the taxpayer's 1952 purchase of 2,164 shares of Wescott Oil stock and liquidation of the corporation, the established rule that a purchase of stock for the purpose of acquiring the corporate assets through liquidation is to be treated as a purchase of the corporate *assets*.

SUMMARY OF ARGUMENT

The facts of record and as found by the District Court indisputably show that the taxpayer purchased

all of the outstanding stock of the Wescott Oil Company (other than the 25 shares he already owned) for the purpose of acquiring the assets of Wescott Oil through liquidation of the corporation (and for immediate resale of the operating assets to the Continental Oil Company pursuant to a prior agreement). It is a well established rule that the purchase of stock for the purpose of acquiring the corporate assets through liquidation of the corporation will be treated simply as a purchase of corporate *assets*, with no effect given to the liquidation. Thus, the District Court erred in holding that taxpayer's gain was realized when and to the extent that he received liquidating distributions from Wescott Oil in the years 1952 and 1953. The taxpayer's purchase of stock and liquidation of the corporation must be treated for tax purposes according to their substance, and thus as a purchase of corporate *assets*, with the result that the taxpayer's gain was realized on his sale of the operating assets to Continental, was in the amount received from Continental less the cost basis allocable to the operating assets, was gain realized in 1952, and, except for the amount attributable to the 25 shares of Wescott Oil stock previously owned, was short-term capital gain.

The District Court's error was apparently in assuming that the case is taken out of the above-mentioned rule because the taxpayer also intended to sell the assets at a profit. But that additional purpose did not change the taxpayer's purpose to acquire the corporate assets; it merely made his purpose to ac-

quire the assets more evident. The District Court erred and should be reversed.

ARGUMENT

The District Court Erred In Failing To Hold That, On the Undisputed Facts of the Case, Tax Consequences Must Be Resolved In the Light of the Established Rule That a Purchase of Corporate Stock for the Purpose of Acquiring the Corporate Assets Through Liquidation of the Corporation Is To Be Treated As a Purchase of the Corporate Assets

Involved here is the purchase of corporate stock immediately followed by a liquidation of the corporation (as well as an immediate sale of the operating assets of the corporation pursuant to a previous agreement). Normally, assets received in liquidation of a corporation are treated as being received in exchange for stock (See Section 115(c) of the Internal Revenue Code of 1939, *supra*), with the result that the stockholders do not realize gain until the amounts (or fair market value of property) they receive on the liquidation exceed the cost basis of their stock. However, there is an established exception to the rule giving effect to liquidating distributions. When corporate stock is purchased for the purpose of obtaining the corporation's assets through liquidation of the corporation, the formalities of the stock purchase and liquidation are ignored and the transaction is given effect according to its substance and thus as a purchase of the corporate *assets*. See *Commissioner* v. *Ashland Oil & R. Co.*, 99 F. 2d 588 (C. A. 6th), certiorari denied, 306 U. S. 661; *Kimbell-Diamond Milling Co.* v. *Commissioner*, 14 T.C.

74, affirmed per curiam, 187 F. 2d 718 (C. A. 5th), certiorari denied, 342 U. S. 827; *Kanawha Gas & Utilities Co.* v. *Commissioner*, 214 F. 2d 685 (C. A. 5th); *Koppers Coal Co.* v. *Commissioner*, 6 T. C. 1209; *Cullen* v. *Commissioner*, 14 T. C. 368; *Snively* v. *Commissioner*, 19 T. C. 850, affirmed on other grounds, 219 F. 2d 266 (C. A. 5th); *Montana-Dakota Utilities Co.* v. *Commissioner*, 26 T. C. 408. In such a case, the stock purchase and liquidation are without tax consequence; the entire transaction merely constitutes a purchase of property from which gain is realized only when and if the acquired assets are sold or otherwise disposed of.

Tax consequences in the present case depend upon whether, as we contend, the District Court erred in failing to apply the latter rule. If applicable here, the taxpayer acquired corporate *assets*, and the fact that he acquired those assets through a purchase of stock and liquidation of the corporation is immaterial and without tax effect. His realization of gain occurred when he sold or otherwise converted those assets. He of course immediately sold the major portion of the assets (the operating assets) to Continental for $1,689,399.07 in cash, so that his gain on the sale is necessarily *short*-term capital gain (except to the extent of the gain, as allowed by the Commissioner, attributable to the 25 shares of stock he had owned since 1945). By selling the operating assets, the taxpayer realized gain in the amount by which the $1,689,399.07 he received in 1952 from Continental exceeded the cost of such operating assets to him. His cost basis for the operating assets was

necessarily that portion of the cost of *all* the assets which is allocable to the *operating assets* or, in other words, the total cost to him of the Wescott Oil stock [3] *less* the fair market value of the other property (102,823.49) which he received in cash or property in the following year (1953). See, e.g., *Graves* v. *Commissioner*, decided May 14, 1952 (1952 P-HT.C. Memorandum Decisions, par. 52,143). Thus, the taxpayer's entire gain from the purchase of the Wescott Oil stock and the liquidation of the corporation was realized in 1952 and was short-term capital gain (except to the extent of the amount attributable to the 25 shares he previously owned), as the Commissioner determined in his deficiency notice, if, as we contend, the taxpayer's purchase of stock and liquidation of the corporation are to be treated as one integrated transaction consisting of a purchase of corporate *assets*.

The District Court's findings of fact make it readily apparent that the taxpayer purchased the stock of Wescott Oil for the purpose of acquiring the assets of the corporation through liquidation. The taxpayer entered into an agreement to sell Wescott Oil's operating assets to Continental even before he approached the other stockholders to buy their stock. (R. 18, 36, 57-59, 125-126, 162-164, 225; Exs. G, H.) Indeed, his stock purchase was financed with the funds he received from Continental for the operating

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[3] We concede that the taxpayer's cost basis includes the $310,123.89 liability of Wescott Oil to the Bank which he personally assumed. See *Montana-Dakota Utilities Co.* v. *Commissioner, supra.*

assets. (R. 38, 125-126, 171-172.) After obtaining options to buy all of the stock, the stock was deposited in escrow and a single stock certificate was issued to the taxpayer. (R. 36-37.) Then, all within three days, the taxpayer, as sole stockholder, called a stockholders' meeting at which it was resolved to liquidate and dissolve the corporation, immediately following that a directors' meeting was also called at which it was resolved to transfer the operating assets to the taxpayer, and taxpayer in turn conveyed those operating assets to Continental. The distribution of the operating assets to the taxpayer and his sale of those assets to Continental occurred all in one day (R. 37-38), with all the essential documents having been prepared in advance (R. 163-166). Liquidation of the remaining assets, totalling $102,861.66, continued into 1953, but there can be no doubt that the taxpayer acquired the corporate stock for the purpose of acquiring the corporate assets through liquidation, so that he could sell the bulk of those assets to Continental. As a matter of fact, he could not have otherwise paid for the stock. Thus, the taxpayer himself testified that his motivating purpose was to secure the assets of Wescott Oil.[4] (R. 173.)

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[4] It may also be noted that what the parties accomplished —a sale of the operating assets to Continental—was exactly what Continental desired but which the parties apparently did not want to effect *directly* because of possible tax consequences. Mr. Wescott had previously negotiated with Continental, but those negotiations broke down not only because Continental was unwilling to pay the price demanded by the Wescott Oil stockholders for their stock (R. 34-35) but

As we interpret the District Court's findings and opinion, the court itself conceded that the taxpayer's purpose was to acquire the corporate assets. The court stated in its findings that the taxpayer "purchased the stock of Wescott Oil Company, not its assets" (R. 43), and of course that is true from the standpoint of *form*. The court also found as a fact that the distribution of corporate assets to the taxpayer "was, of course, an essential part of his plan of liquidation." (R. 45.) The court further found that the taxpayer did not acquire the stock "solely" in order to acquire Wescott Oil's *operating* assets, since the taxpayer "was interested in the operating assets of the company only insofar as they were part of his over-all plan to liquidate the company at a profit." (R. 45.) In its opinion the District Court also stated that the taxpayer purchased the stock

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because Continental was interested only in buying the assets, that is, the operating assets, of Wescott Oil (R. 36-38, 104-105, 150-151). And Mr. Wescott testified that he had been too well informed taxwise to consummate the transaction in the latter fashion because of the adverse tax consequences which would follow therefrom, and that his tax attorney had advised him "not to do that". (R. 104-105.) They were quite obviously concerned lest both the corporation and the individual stockholders (then including Mr. Wescott, the taxpayer, and others), as distributees, would be required to pay income tax on the profits from such a sale (Cf. *Commissioner* v. *Court Holding Co.*, 324 U. S. 331), and the record shows that the taxpayer continued thereafter to be much concerned about this possibility, as indicated by his repeated attempts to secure the advice of tax counsel in respect of the tax effects of the transaction, both in respect of "My [personal] tax matters," and also those of Wescott Oil. (R. 135-137, 167-169, 193-194.)

"intending to liquidate the corporation, sell the assets, and thereby make a profit." (R. 28-29.)

We are therefore somewhat at a loss to understand why the District Court did not apply the well-settled rule that a purchase of stock for the purpose of acquiring the corporate assets through liquidation is to be treated according to its substance and thus as a purchase of the corporate assets. On the facts as found by the court, it is indisputable that the taxpayer purchased the stock of Wescott Oil for the purpose of liquidating the corporation and thereby acquiring the assets of the corporation. That he also intended to sell those assets when he acquired them, and at a profit, does not change the fact that his stock purchase and liquidation of the corporation were integrated parts of a plan to acquire the assets. Had he not sold the operating assets to Continental, his stock purchase and liquidation of the corporation would not have resulted in the realization of gain, but it would still be treated as a purchase of *assets.* See *Commissioner* v. *Ashland Oil & R. Co., supra; Kimbell-Diamond Milling Co.* v. *Commissioner, supra; Kanawha Gas & Utilities Co.* v. *Commissioner, supra; Snively* v. *Commissioner, supra; Cullen* v. *Commissioner, supra; Koppers Coal Co.* v. *Commissioner, supra; Montana-Dakota Utilities Co.* v. *Commissioner, supra.* The principle involved here is that a stock purchase for the purpose of acquiring the corporate assets through liquidation of the corporation eliminates the liquidation of the corporation as a taxable event, there being no real exchange of stock for assets of the corporation,

and postpones the taxable event until there is a sale or other disposition of the assets. The fact that the taxpayer planned to sell and in fact sold the operating assets to Continental resulted in the realization of gain by him in a transaction which has nothing to do with his purpose to acquire the assets other than to make the latter purpose all the more evident; it did not change that purpose. Thus, if the District Court thought otherwise, as indicated at one point in its opinion (R. 29), the court was in error.

On the question of whether the taxpayer's stock purchase and liquidation of the corporation are to be given effect simply as a purchase of corporate assets, the District Court's decision is plainly contrary to the pertinent decisions. The applicable rule was first enunciated in *Commissioner* v. *Ashland Oil & R. Co.*, *supra*, where the question was as to the cost basis, for depletion purposes, of the acquired assets. There one corporation (Swiss) had originally attempted to buy outright the properties of another corporation (Union) but Union refused to sell because (as shown in the dissenting opinion, p. 593) it would have been required to pay tax on the profit—just as would have been the situation had Wescott Oil sold outright to Continental in the instant case (R. 104-106). Hence, the stockholders of Union agreed to give Swiss an option to purchase all the stock of Union for a stipulated price. The stock was to be placed in escrow and Union was to continue to operate the property until the net proceeds from operations equalled $1,000,000 which was to be paid to the stockholders of Union. The stock was

then to be delivered to Swiss by the escrow agent. The sale of stock was to carry with it only the oil and gas leases owned by Union, the balance of the assets to be distributed to Union's stockholders. Union's stockholders were also to assume Union's liabilities. Upon delivery of the stock to Swiss, Union was liquidated, and the oil and gas leases were distributed to Swiss which then used them in its business. The Commissioner attempted to tax the gain derived by Swiss upon the liquidation of Union. The taxpayer contended successfully there, however, that the acquisition of Union's stock and the liquidation of that corporation were merely steps in a unitary plan to acquire Union's oil producing properties, and that no taxable gain was realized since the properties were still owned by it. The court found from a consideration of all the circumstances of that case that Swiss' dominant purpose in entering into the agreement was to acquire the oil and gas properties of Union and, upon thus finding that the liquidation of Union was an intermediate step in a unified plan to acquire its properties, the court refused to impose a tax upon the liquidation step by recognizing gain thereon. Rather, the court held that the transaction should be viewed as a whole, that the purchase of stock was merely a step in the acquisition of the corporate assets, and that the purchasers' basis for depletion was the cost of the stock to it. In deciding in favor of the taxpayer, the court noted that the exhibits and witnesses in the case fully disclosed Swiss' plan to secure Union's properties. The court stated (p. 591):

It has been said too often to warrant citation that taxation is an intensely practical matter, and that the substance of the thing done and not the form it took must govern. This principle has been repeatedly invoked by the Commissioner and applied by the Board. *Carter Publications, Inc.* v. *Commissioner*, 28 B.T.A. 160; *Warner Co.* v. *Commissioner*, 26 B.T.A. 1225; *George Whittell & Co., Inc.* v. *Commissioner*, 34 B.T.A. 1070. And without regard to whether the result is imposition or relief from taxation, the courts have recognized that where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole, and closely related steps will not be separated either at the instance of the taxpayer or the taxing authority. *Prairie Oil & Gas Co.* v. *Motter*, 10 Cir., 66 F. 2d 309; *Tulsa Tribune Co.* v. *Commissioner*, 10 Cir., 58 F. 2d 937, 940; *Ashles Realty Corp.* v. *Commissioner*, 2 Cir., 71 F. 2d 150; *Helvering* v. *Security Savings Bank*, 4 Cir., 72 F. 2d 874.

* * * *

It is not decisive that the purpose of Swiss to acquire the Union properties is not recited in formal agreements executed to bring about that result if such purpose is disclosed by circumstances which beyond controversy proclaim it. Nor does the fact that the Union stock was held by Swiss for almost a year destroy the transitory character of such holding when the terms of the contract are considered.

In the District Court the taxpayer attempted to distinguish the *Ashland* case on the ground that it involved a hybrid transaction, asserting that the

provision attaching only to the oil and gas properties of Union makes it impossible to apply the *Ashland* rule to a situation, such as that in the instant case, where the purchaser of the stock acquires all the rights and liabilities normally attendant upon stock ownership. While it is true that Swiss, in purchasing Union's stock, acquired neither all of its assets nor any of its liabilities, yet this in itself is clearly not a sufficient reason for refusing application of the rule of the *Ashland* case to the situation where the purchaser of the stock acquired rights in all of the corporation's assets and liabilities, providing it is equally clear that the essential nature of the transaction is the acquisition of property, as here. The factual distinction alleged actually makes the instant case an *a fortiori* proposition. The formalism of a liquidation distribution could not be used in *Ashland* to successfully deflect the proper incidence of taxation, nor can it here. The crucial point is, of course, that in cases of this sort the liquidation is not given effect, since the ultimate factual result of a purchase and sale of all the stock of a corporation and the liquidation of that corporation shortly thereafter is, in substance and for tax purposes, merely a purchase of the corporate assets.

In *Kinbell-Diamond Milling Co.* v. *Commissioner*, *supra*, the taxpayer-corporation had suffered the loss of its plant by fire and recovered the insurance thereon. Its board of directors resolved to use the insurance proceeds to acquire the stock of another corporation (Whaley) which was engaged in the same business. The resolution recited that as soon as

the stock was obtained Whaley would be liquidated and all of its assets distributed to the taxpayer. Its primary object, of course, was to obtain Whaley's plant to replace its own. The question before the court there was whether the taxpayer was entitled to use Whaley's cost basis as its basis for the assets acquired from Whaley, as it urged, or whether, as the Commissioner contended, its basis in the assets was the cost of Whaley's stock. The Tax Court had held that the taxpayer's proper basis in the assets was its cost in obtaining Whaley's stock. In so holding, it was necessary for the Tax Court to pass on the taxpayer's contention that it was entitled to Whaley's basis in the assets because the acquisition of Whaley's stock and its subsequent liquidation were two separate transactions. From an examination of the minutes of the meetings of the taxpayer's board of directors and from the document evidencing the program of the complete liquidation of Whaley, however, the Tax Court determined that the only intention the taxpayer ever had was to acquire Whaley's assets, and thus, relying on the *Ashland* case, *supra*, it stated (p. 80):

> We hold that the purchases of Whaley's stock and its subsequent liquidation must be considered as one transaction, namely, the purchase of Whaley's assets which was petitioner's sole intention.

The Fifth Circuit affirmed *per curiam*, *supra*, and hence this case as well as the other analogous decisions above-cited hold generally that, where the substance of a transaction is the purchase of assets, the

corporate liquidation step in the process is to be ignored in determining the tax effect of the transaction, even where the purchaser of stock acquires all the rights and liabilities normally constituting stock ownership, and even where there appear to have been no negotiations, preceding the stock-purchase plan, for the purchase of the assets directly.

In a number of other cases involving variant factual situations the courts have held that the component parts of a single transaction cannot be treated separately for the purpose of levying income taxes. For instance, in *Mather* v. *Commissioner*, 149 F. 2d 393 (C. A. 6th), certiorari denied, 326 U. S. 767, it was held that residuary legatees of an accommodation indorser of a note who, through the transfer of the assets of the estate to a corporation and its subsequent liquidation, paid the balance owing on the note, were not entitled to a bad debt deduction. In ignoring the transfer to the corporation, the court stated (p. 397):

> * * * and the courts have recognized that where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole, and closely related steps will not be separated either at the instance of the taxpayer or the taxing authority.

See also, *Tulsa Tribune Co.* v. *Commissioner*, 58 F. 2d 937, 940 (C. A. 10th); *Ahles Realty Corp.* v. *Commissioner*, 71 F. 2d 150 (C. A. 2d); Paul, Selected Studies in Federal Taxation (2d Series), pp. 205-214.

In view of the foregoing, it is clear, we submit, that, on the facts of record and in the light of the authorities above cited, the taxpayer acquired the stock of Wescott Oil for the purpose of obtaining its assets, through the liquidation of the corporation (for immediate resale of the operating assets to Continental), and, accordingly, that the transaction must be given effect according to its substance, that is, as a purchase of the corporate *assets* by the taxpayer. It follows that, contrary to the District Court's holding, all of the gain realized by the taxpayer in the transaction in question (with a small exception as specified in the record) is taxable as short-term capital gain for the taxable year 1952.

CONCLUSION

The judgment of the District Court is incorrect and should be reversed.

Respectfully submitted,

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MAY, 1959.

APPENDIX

Schedule of exhibits identified, offered and received or rejected as evidence.

Taxpayer's Exhibits [5]	Identified	Offered	Received in Evidence	Rejected
A	R. 17, 57-59	R. 57-59	R. 17, 57-59	
B	R. 17, 57-59	R. 57-59	R. 17, 57-59	
C	R. 17, 57-59	R. 57-59	R. 17, 57-59	
D	R. 17, 57-59	R. 57-59	R. 17, 57-59	
E	R. 17, 57-59	R. 57-59	R. 17, 57-59	
F	R. 18, 57-59	R. 57-59	R. 18, 57-59	
G	R. 18, 57-59	R. 57-59	R. 18, 57-59	
H	R. 18, 57-59	R. 57-59	R. 18, 57-59	
I	R. 18, 57-59	R. 57-59	R. 18, 57-59	
J	R. 18, 57-59	R. 57-59	R. 18, 57-59	
K	R. 18, 57-59	R. 57-59	R. 18, 57-59	
L	R. 18, 57-59	R. 57-59	R. 18, 57-59	
M	R. 18, 57-59	R. 57-59	R. 18, 57-59	
N	R. 18, 57-59, 143	R. 57-59	R. 18, 57-59	
O	R. 19, 57-59	R. 57-59	R. 19, 57-59	
P	R. 19, 57-59	R. 57-59	R. 19, 57-59	
Q	R. 19, 57-59	R. 57-59	R. 19, 57-59	
R	R. 59-60	R. 59-60	R. 59-60	
S	R. 60	R. 60	R. 60	
T	R. 60	R. 60	R. 60	
U	R. 60-61	R. 60-61	R. 60-61	
V	R. 61	R. 61	R. 61	
W	R. 63	R. 66	R. 66	
X	R. 63-64	R. 67	R. 67-68	
Y	R. 64	R. 68	R. 68-69	
Z	R. 119	R. 121	R. 121	
AA	R. 142	R. 143	R. 143	
Government's Exhibit				
#1	R. 198-199			R. 200-201

[5] The taxpayer's exhibits A-Q were initially stipulated by the parties to be identified and received as evidence (R. 17-19, 57-59).

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